

# Peru's Interoceanica 4 road: the Brazilian connection

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In late April, Brazil's construction champions Camargo Correa, Andrade Gutierrez and Queiroz Galvao once again stormed the transport market in Peru with the financial close of the US\$562 million Intersur toll road

Intersur is the fourth segment of the southern part of a road network promoted by 12 South American governments known as the Initiative for the Integration of Regional Infrastructure in South America (IIRSA). The programme was established in 2000 to develop and implement priority infrastructure projects critical to the region's economic development.

In Peru, IIRSA - also known as the Interoceanica - entails a network of 2,600km of existing and yet-to-be-built roads that will connect port cities in the country with those in Brazil.

Segments 2 and 3 or IIRSA Sur closed last year and involved the construction, upgrade and maintenance of more than 700km, while segments 1 and 5 with distances of 757km and 767km respectively are currently under tender.

The Interoceanica in northern Peru is known as IIRSA Norte, a 906km toll road that reached financial close in August 2006. In central Peru another road is also currently under tender the 867km IIRSA Centro road.

## The project

Intersur is a 306km greenfield road project that runs from the Inambari bridge in the Amazon Province of Madre de Dios to Azangaro in the southern Andean Province of Puno. When completed, it will span southern Peru, Bolivia, and northwest Brazil.

ProInversion, Peru's investment promotion agency responsible for conducting the tender process received the project from the ministry of transport (MTC) on the 26 of November 2004. On 19 of January 2005, the agency launched the tender and on 23 of June 2005 the project was awarded to the consortium Intersur Concesiones made up of:

- Andrade Gutierrez (33.33%)
- Camargo Correa (33.33%)
- Queiroz Galvao (33.33%)

Once the third and final version of the 25-year concession contract was agreed by the sponsors, ProInversion, the MTC

and the ministry of economy; contract signing followed on 4 August 2005. Although the concession awarder is ProInversion, the contract was signed between the MTC and the concessionaire.

The project will be built under a BOT arrangement and works have to be completed according to the following milestones:

- Stage 1 construction of 29 per cent of the project in 1 year and half from July 2006
- Stage 2 construction of 35 per cent of the project in year 3
- Stage 3 completion in year 4 (2010)

OSITRAN, Peru's regulatory agency for transport infrastructure is the body responsible for monitoring construction progress. Toll booths will be built every 100km.

Payments are subject to completion of the milestones in the form of the sale of certificates of annual construction payments (certificados de reconocimiento de derechos del pago anual por obras - CRPAOs) to be issued by the government of Peru (GOP).

#### The financing

It was clear from the beginning that, like the other IIRSA roads, Intersur could not be expected to generate sufficient toll revenues to meet its construction costs - so the government stepped in.

Mark Salgado, analyst at Fitch Ratings says 'The IIRSA toll road network is of strategic importance to Peru and it has other benefits outside toll revenues. So the GOP decided to finance these roads with CRPAOs.'

The three IIRSA projects so far have all been financed via bonds or to be more precise by the securitisation of CRPAOs. These CRPAOs are essentially work progress payments.

On completion of every section of the road, the concessionnaire is entitled to a CRPAO from the government. This certificate is fully transferable, subject to New York law, and once generated, represents an obligation of the GOP to pay the concessionnaire a fixed semi-annual sum in US dollars irrespective of any factors relating to the road (e.g. traffic volume).

According to the terms of the deal, whenever a CRPAO is generated, it will be sold to the bond issuer, on a purchase agreement basis. By this method, the total amount of funds from the bond issue is gradually disbursed to the concessionnaire, while the bond is gradually amortised through the revenue from CRPAOs.

Salgado from Fitch says 'Each CRPAO constitutes an unconditional and irrevocable obligation of the GOP. Therefore, our view is that the GOP is the ultimate payer'.

The 144A zero coupon bonds were issued in two tranches by the project vehicle, Interoceanica IV Finance Limited:

- Series 2007-1 US\$324 million maturing in 2025
- Series 2007-2 US\$238 million maturing in 2018

Fitch rated the bonds BB+, while Moody's assigned it Ba3. Both agencies hailed the importance of CRPAOs in achieving this rating. Although legally distinct from public debt, CRPAOs are incorporated in the national budget as line-up items in

the ministry of finance and the ratings agencies were satisfied that the likelihood of the government honouring one obligation over the other was minimal.

The bonds were placed in Peru and in the international capital markets with pension funds both at home and abroad buying most of the paper.

BNP Paribas was the bond arranger. It used a credit default swap placed by Goldman Sachs to provide a measure of security for the sponsors in the event of an budgeting error. This allows the concessionnaire to receive a payment the size of a whole semiannual CRPAO that they have sold to the issuer in advance of scheduled submission dates. In addition to this some security for noteholders was provided in the form of a total return swap placed by Goldman Sachs, by which all monies not invested in the purchase of CRPAOs are to be invested in positions which earn a fixed rate of return and which are fully convertible in the event of a termination event occurring.

A termination clause would be triggered if six months had elapsed after the scheduled purchase date of a CRPAO without completion of the relevant construction phase. In this situation noteholders would receive all issuance proceeds which had not been used in the purchase of CRPAOs, and the proceeds invested in the total return swap, as well as compensation from the sponsors in the form of a make-whole payment if it was deemed to be be their fault. In this way, noteholder exposure to construction risk is mitigated considerably.

The sponsors received legal advice from Clifford Chance, while Milbank advised BNP Paribas.

Conclusion

With every southern province in Peru wanting a piece of the Intersur, the closing of the project reflects considerable investment in time and effort on the part of the Peruvian Government in trying to keep all parties satisfied.

The deal also represents a victory for the consortium who managed to achieve a rating equivalent to Peruvian national debt through intelligent hedging and the flexible purchase schedule set for the obligation certificates issued by the Republic of Peru.

It also paves the way for the final two instalments of the Interoceanica: San Juan de Marcona - Urcos and Matanari - Azangaro, Ilo - Juliaca. So far, all the previous IIRSA financings have used different hedging mechanisms; the total return swap, a cash management agreement, and a credit-linked note, respectively. It will be interesting to see what innovations surface in the fourth.

The project at a glance

Project Name	Intersur Concesiones S.A.
Location	Peru
Description	A 306km long tolled highway from Inambari to Azangaro.
Sponsors	Andrade Gutierrez - (33.3%)
	Queiroz Galvao (33.3%)
	Camargo Correa - (33.3%)
EPC Contractor	Andrade Gutierrez, Queiroz Galvao, Camargo Correa
Project Duration (Including construction)	15 years
Construction Stage	4 years
Total Project Value	US\$ 562 million
Total senior debt	US\$ 562 million

Senior debt breakdown	Series 2007-1 US\$ 324 million maturing in 2025
	Series 2007-2 US\$ 238 million maturing in 2018
Coupon	0 per cent per annum (4.1 per cent implied rate of return)
Bookrunner	BNP Paribas
Legal Adviser to sponsor	Clifford Chance
Legal adviser to banks	Milbank Tweed
Date of financial close	26 April 2007

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